

**PEER REVIEW OF PROGRESS ON
ECONOMIC INSTRUMENTS STUDY**

**Egyptian Environmental Policy Program
Program Support Unit**

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February 8, 2001

A. Review of Work to Date

1. There exists a consensus that progress to date has been slower than desired and a concern that the study goals may not be achieved.
2. The initial Terms Of Reference needed substantial clarification before productive work could begin. As originally conceived, the international consultant was to spend 30 days on the project and delegate most of the work to local consultants. This plan proved unworkable for a number of reasons. The most important difficulty was in communicating an understanding of economic instruments (EIs) to the local consultants so that their work was effective.
3. The project started with efforts to develop a work plan and to produce an Economic Instrument Description form. While these activities seemed reasonable at the time, in retrospect this slowed progress substantially as different project participants labored under different perceptions of what constituted an economic instrument and what economic instruments could accomplish. More helpful in the beginning would have been a concise review of international experiences with the use of EIs in developing nations. The review would help to clarify the nature and functions of such instruments and would aid in identifying applications in Egypt.
4. The Economic Instrument Description (EID) form is well intended and has many desirable attributes but does not appear to be very useful as a screening device for identifying EIs in use in Egypt. In addition, the form is quite challenging to complete, a factor that has slowed progress on the study. Replacing the EID form with a short check list would suffice for the initial screening step. Only instruments that pass an initial screening that polluters are being made to pay in some fashion should be subject to further analysis.
5. The review of EIs in use in Egypt is incomplete. While EIs (especially environmentally unfriendly subsidies) may be difficult to identify, the approach of assigning this task primarily to a local consultant appears not to have worked well. The international consultant needs to stay closely involved in these efforts (including participating in interviews with individuals at many levels of government and civil society) to assure the efforts to identify instruments are effective.
6. The working group has several members who are very well informed on the topic of EIs and could be a valuable asset, yet the full group apparently has met only two or three times and the meetings produced little constructive information about instruments. Most of the attention of the group was devoted to procedural matters, not substance. Greater preparation for the workgroup meetings, more frequent workgroup meetings, and email contact between meetings should help to increase the productivity of the working group. Additionally, all members of the working group should be consulted individually to solicit views and information.

7. The complex institutional and cultural context in which EIs must be implemented and the failed attempts of other donor efforts to design and implement EIs argue that there must be great familiarity with institutional and cultural factors to design workable instruments in Egypt. Extensive contact with government officials outside EEAA and with the community that would be affected by an EI is essential before EEAA could move forward with an initiative. This contact has not been taking place. Also, the approach taken by the international consultant has been more rigorous and detailed than desirable given the time and resources available for the study.
8. The PSU's study manager has been assigned to supervise at least ten separate activities and does not have the time to schedule meetings make contacts and do the all the extensive in-country work necessary to make this study a success. He can provide oversight but cannot be expected to serve as a backstop to the many logistical, technical and other requirements for the study, nor to provide intellectual quality control on the documents that are being produced.
9. The FINBI TOR was difficult to follow and could be improved greatly, especially in view of the fact that FINBI is not familiar with the subject matter. FINBI appears to have useful skills and contacts, but it was premature to engage FINBI for significant work until the review of existing EIs was completed and concrete policy proposals were being considered. The problem was recognized in mid November when a stop-work order was issued by the PSU study manager.
10. Cooperation and coordination with other USAID-funded projects is problematic. For example, Cairo air quality is a key environmental problem identified by the NEAP and the most important area for EI development, yet the CAIP will not share any results of their work on the Cairo emission inventory, source attribution or monitoring.

B. WORK PLAN

The tasks of the work plan, the first study output, seem to be laid out reasonably well. Here are comments on Phase I of the work plan and the accomplishments to date toward the specific tasks.

1. Identify and describe economic instruments currently in use in Egypt in the environmental and tourism sectors and instruments in other sectors that would have an effect on the environmental sector e.g., investment incentives.

This is a useful task, however it probably would more logically come after the review of pertinent international experiences. As argued earlier, the availability of an international review would make it easier to identify instruments in use in Egypt.

Another preliminary task that has not been done is to characterize briefly the types of environmental issues that can be addressed with an EI. Once of the recommendations is directed at this issue.

Article 17 of Law 4 refers to economic incentives that EEAA could provide to firms as an incentive to engage in environmental protection. A legal interpretation may suggest that this includes transfers such as technical information, education and performance awards and recognition probably are within EEAA's charter. In fact, EEAA has some initiatives underway along such lines. These initiatives should be reviewed to see if they could be classified as existing EIs and perhaps modified slightly to make them more effective in harnessing market forces. Other, more traditional economic instruments, such as emission fees, marketable permits and deposit refund systems are not mentioned in Law 4. This argues that EEAA would require a great deal of cooperation from affected ministries and industries to go forward with initiatives such as fees, charges and taxes, or reducing existing subsidies.

Among the EIs that apparently are already in place in Egypt (and not referenced in the study outputs to date), the following probably should be mentioned, even if not analyzed in any detail:

- The current system of fines and penalties for natural resource damage.
- Egypt's pollutant release and transfer reporting (PRTR) activities with OECD.
- Environmentally harmful subsidies such as those that existed until recently for pesticides and fertilizers, and below cost charges for water and wastewater service to farms, firms and households.
- NGO environmental education and information activities.
- EEAA information and education activities.

Instruments whose implementation in Egypt appears to be imminent:

- Debt for environment swaps
- Debt for nature swaps
- Clean Development Mechanism

2. Identify existing and potential legal, policy, institutional, and administrative constraints that might impede the introduction of new instruments or mechanisms but do not limit consideration of candidate EIs to only those that satisfy the current constraints.

No extended discussion of these issues could be found in the study documents. A legal analysis was delivered recently, but it consists mainly of a compilation of the provisions of various laws and regulations and includes less than one page of what one might term analysis. There is virtually no discussion of what may be possible. Many issues could be productively explored:

- Are there legal barriers to the use of emission averaging or trading as a means of reducing compliance costs?
- Are there legal barriers to the implementation of a PRTR system or environmental labeling in Egypt?
- Does EEAA have the legal authority to create voluntary pollution prevention programs and to offer technical assistance to participating firms?

A review of institutional and administrative considerations has not been produced, nor does it appear to be under investigation at present.

It would be very useful to include previous attempts to introduce EIs, even when the attempts ultimately failed, for they offer insight into administrative, political and institutional problems that must be overcome. Consider for example EEAA's proposal to create a method for publicly disclosing firms that were found to be in violation of emission and effluent standards. The proposal failed because of opposition from powerful ministries that oversee, operate, supply to or buy from firms that would be affected. A special concern was the negative impact such a proposal could have on privatization efforts.

3. Prepare a template for systematically describing candidate EIs and the advantages and disadvantages from an environmental, economic, and administrative point of view.

Is this the EID --- which doesn't seem responsive to the task, or is something new to be forthcoming? More criteria than environmental, economic and administrative aspects should be explored. These criteria can be divided into two groups. The first set of evaluative criteria concern the intrinsic characteristics of a particular economic instrument (EI) which can be evaluated along the following lines:

- Economic efficiency or cost-saving potential. What are the real resource savings from using an economic instrument rather than doing nothing or using some other alternative?
- Environmental effectiveness. Does the economic instrument provide the same or greater protection of the environment than an alternative? If there are uncertainties, what are the tradeoffs between cost savings and potential environmental degradation?
- Distributive effects. Who bears the financial costs of the economic instrument approach? What are the distributive effects under the alternative? How are environmental gains distributed by income group and by location of the groups under the EI and alternative approaches?
- Revenue raising. What impact does the economic instrument have on governmental budgets? How does this compare to other regulatory approaches?
- Technological change and innovation. Sometimes termed "dynamic efficiency, this criterion asks whether the mechanism for securing environmental improvement is likely to stimulate the search for more effective and/or less expensive means of pollution control. Do the other regulatory alternatives offer any stimulus to innovation and technical change?

A second set of criteria is related more to the institutional setting in which economic instruments or regulatory alternatives would be instituted. These implementation criteria include:

- Political acceptability. Who might be opposed and what obstacles would this present? Who would favor the economic instrument approach? Is there a broad base of “winners”, how large are the individual gains, are there a small number of “losers” but which much to lose who are likely to be very vocal about their losses?
- Institutional capacity. What additional burdens, if any, would an economic instrument approach place on the government’s capabilities and capacities compared to the alternatives?
- Legal framework. Are existing laws adequate or would new legislation be required? If new legislation would be needed, what is the prognosis for successfully passing it?
- Administrative ease of implementation. Would new regulations be required for the EI? How much effort would be required? What about monitoring requirements? How would compliance be accomplished and what will be the likely enforcement requirements?
- Are there successful applications of the candidate instrument in other nations? What does that record in other countries reveal regarding probable institutional burdens, potential pitfalls, and the ultimate probability of successfully implementing an EI?

4. Compile a working list of candidate EIs and fill out the template for each candidate EI. Selection of candidates will be based in part on review of the sectors and pollutants identified by the NEAP process as high priority. Candidates can include possible changes to existing economic instruments (including revenue instruments).

Work does not seem to have progressed to this stage but the task certainly is reasonable.

5. Conduct a series of meetings to discuss existing instruments, clarify constraints, explore interest in new instruments, review the initial list of EIs, and select a subset of EIs to be recommended as part of an overall EI strategy. The sub-set selected should include a list of intermediate term EIs and longer term EIs.

Not yet at this stage. Only comment is that the nature of the meetings is not specified. Does it refer to the working group, some focus group, or something else?

6. Propose an overall strategy in the form of a draft report for the introduction of economic instruments with the rationale for following such a strategy based on the selected subset of EIs and the description of each of these candidate EIs in the template that has been filled out for them.

This is quite reasonable.

Phase II – Detailed Evaluation and Implementation Planning

The Phase II plan seems reasonable at this stage, but may need to be revisited as work progresses to determine that it still applies fully.

1. After the Phase I draft strategy report has been reviewed, evaluate a limited number specific designs for economic instruments selected for the overall strategy that could be introduced in

Egypt. At a minimum, the analysis should include an evaluation of proposed instruments in terms of a set of *ex ante* criteria such as net-benefits, and effects associated with use of revenues produced by environmental taxes and source of revenues for environmental subsidies. The evaluation will also discuss anticipated incentive effects and magnitude of revenue that would be generated if the instrument were implemented.

2. Each candidate EI design that achieves a successful evaluation will be the subject of an implementation study. This study should discuss the steps needed to implement the proposed instrument design and suggest a practical program for establishing necessary collection, accounting, reporting, enforcement, disbursement, monitoring, and post-implementation evaluation analyses.
3. *Prepare a draft report on each EI covered by Tasks 1 and 2 above and present this report with recommendations at a seminar organized by the PSU.*
4. Convene follow-up meetings with counterparts, USAID, other donors, and stakeholders to elicit feedback on the draft reports.
5. Finalize the detailed evaluation and implementation planning reports.

Phase III Implementation of Economic Instruments

Assist EEAA in the implementation of the Economic Instruments that have been selected as part of the overall EI strategy and have been recommended for implementation in Phase II.

C. EID Form

The form requests more detail than necessary to understand existing instruments and far too much detail to serve as a screening device. A simpler check list for screening purposes and initial discussion of new initiatives would include:

- Brief description of the instrument
- Presumed intent of the instrument
- Does it satisfy the polluter pays principle?
- Are there any special features instrument or studies that have been done on this instrument?
- Key people to contact for more information

D. Future Activities

- Focus this study on modifying existing instruments (or reducing environmentally harmful subsidies) as this is likely to be easier than implementing wholly new instruments. The study now is headed in this direction.
- Directly involve the international consultant in producing a comprehensive list of existing instruments in use in Egypt. The categories probably should include: (1) charges, fees and taxes that have positive or negative environmental consequences; (2) emission/effluent averaging requirements or trading; (3) deposit-refund systems; (4) subsidies (both those that are beneficial to the environment and those that are harmful); (5) liability for pollutant releases that harm the environment and natural resources; (6) information disclosure such as pollutant release or environmental labeling; (7) voluntary pollution prevention activities. The descriptions of every instrument need not be detailed. The longer is the list the more useful it will be to illuminate policy development by EEAA and the greater will be the opportunities in the study to develop fall-back initiatives if the first few proposals encounter obstacles.
- The review of international experiences should not be done in Egypt. Not only are research materials more limited, but the consultant(s) should spend all time in country dealing with Egypt-specific issues.
- Identify new instruments for potential use in Egypt based on successful international experiences. This list of potential new instruments would be mainly for purposes of future study and discussion, though one or two might be put forward as new initiatives.
- Increase the time the international consultant spends in Egypt and make sure considerable effort is devoted to discussing and promoting the initiatives outside of EEAA.
- Extend the deadline for completing this study by 6 weeks to allow for more time in-country by the international consultant.
- Involve the full working group more as active participants; use them as a sounding board for new ideas and keep them regularly updated on progress through email if not monthly meetings.
- Ask USAID to facilitate improved cooperation and coordination among USAID-funded projects.
- It would help to identify what EIs can accomplish and explain that to the working group and to others who are interviewed during the course of this project (e.g., cost saving, addressing environmental problems not amenable to command and control, encouraging pollution reductions beyond what can be done through command and control, stimulating development and adoption of less polluting technologies by firms and individuals). This would help to identify the types of problems in Egypt that already are being addressed or could be addressed and should help the team and the working group to stay focused.